#### **CHAPTER 5**

#### 5-000 INCURRED COST PROPOSALS

#### 5-101 Incurred Cost General

This chapter covers submission of incurred cost proposals. These would include the various indirect overhead and General and Administrative (G&A) rates which could be found at a contractor. The incurred cost proposal encompasses both the indirect cost pool and base costs applicable to a submitted rate.

#### 5-201 Contractor Proposal

The "Allowable Cost And Payment" clause (FAR 52.216-7) requires that the contractor prepare an incurred cost proposal together with supporting data, within 90 days after the end of its fiscal year. An illustration of an incurred cost proposal follows. The receipt of a proposal by the audit office starts the audit process. This proposal should include a signed "Certificate of Indirect Costs" in accordance with FAR 42.703-2. A copy of this certificate may be found at FAR 52.242-4. (See Schedule L of the model incurred cost proposal under section 5-701 of this pamphlet.) An adequate proposal should reduce the time required to do the audit because numerous preliminary steps can be performed before the auditor(s) arrives at the field location.

#### 5-202 Penalties for Mischarging

a. The manipulation of charges to a contract may be subject to criminal penalties under 18 United States Code (U.S.C.) 1001, which reads as follows:

Whoever, in any matter within the jurisdiction of any department or agency of the United States knowingly and willfully falsifies, conceals or covers up by any trick, scheme, or device a material fact or makes any false, fictitious or fraudulent statements or representations, or makes or uses any false writing or document knowing the same to contain any false, fictitious or fraudulent statement or entry shall be fined not more than \$10,000 or imprisoned not more than five years, or both.

b. Penalties will be assessed against contractors who include expressly unallowable costs, or costs previously determined to be unallowable for that contractor, in a final indirect cost rate proposal, pursuant to 10 U.S.C. 2324 (a) through (d) and 41 U.S.C. 256 (a) through (d). Implementing guidance for these statutes is currently provided in FAR 42.709 and was effective for all contracts on 1 October 1995. Guidance was previously in DFARS 252.231-70 for DoD cost-type and fixed-priced incentive fee contracts in excess of \$100,000 issued after 26 February 1987.

#### 5-301 Audit Evaluation

- a. After receipt of an adequate proposal, the auditor will contact the contractor's representative and set up an entrance conference. If the proposal is inadequate, the auditor will notify the contractor of the deficiency. Absent some mutually agreeable workaround arrangement, the audit will likely be delayed pending receipt of the necessary documents. The auditor may also have performed certain analyses and tests of the books and records during the fiscal year the costs were actually being incurred that will supplement the audit work performed after receipt of the proposal.
- b. The audit will include both direct and indirect costs. The audit objective is to examine contractor cost representations (i.e., public vouchers, incurred cost proposal, etc.) to express an opinion as to whether such costs are: reasonable, allocable to the contract(s), in accordance with generally accepted accounting principles (GAAP) and Cost Accounting Standards (CAS), and not prohibited by the contract, Government statute, or regulation (see FAR 31.201-2).
- c. After completing the audit, the auditor will discuss the results of audit with the contractor and provide the contractor a copy of the draft audit report. The contractor's comments will be included in the final report. If the rates are auditor determined, once agreement is reached on the indirect rates, the contractor will be asked to sign an audit-furnished indirect rate agreement. If agreement with the contractor is not reached, DCAA will forward its audit report concerning the rates to the cognizant contracting officer who will then resolve the disagreement. The auditor will also issue a DCAA Form 1 to recover any reimbursement of unallowable costs that have occurred. The contractor may appeal the Form 1 disallowance to the contracting officer or file a claim under the contract "Disputes" clause (FAR 52-233-1). If rates are to be negotiated by the contracting officer (CO), the audit report and contractor comments will be forwarded to the contracting officer for action.

#### 5-401 Direct Costs

FAR 31.202 defines direct costs as any cost that can be identified specifically with a particular final cost objective (i.e., cost incurred for a specific contract).

#### 5-501 Indirect Costs

FAR 31.203 defines an indirect cost as any cost not directly identified with a single, final cost objective, but identified with two or more final cost objectives or an intermediate cost objective. It is not subject to treatment as a direct cost.

# 5-601 Facilities Capital Cost of Money (FAR 31.205-10)

a. Facilities Capital Cost of Money (cost of capital committed to facilities) is an imputed cost determined by applying a cost of money rate to facilities capital employed in contract performance. It is allowable whether or not the contract is otherwise subject to cost accounting standards (reference 48 CFR Chapter 99) if:

- (1) the contractor's capital investment is measured, allocated to contracts, and costed in accordance with CAS 414;
- (2) the contractor maintains adequate records to demonstrate compliance with this standard;
- (3) the estimated facilities capital cost of money was specifically identified or proposed in cost proposals relating to the contract under which this cost is to be claimed; and
- (4) the requirements of FAR 31.205-52, which limit the allowability of facilities capital cost of money, are observed.
- b. The facilities capital cost of money need not be entered on the contractor's books of account. However, the contractor shall make a memorandum entry of the cost and maintain, in a manner that permits audit and verification, all relevant schedules, cost data, and other data necessary to fully support the memorandum entry. An example of a facilities capital cost of money submission can be found in Section 5-701 (Schedule D).
- c. There is no requirement for a contractor to propose facilities capital cost of money in pricing and performing a contract. If it chooses not to propose this cost during contract pricing then the contractor waives any right to claim it during contract performance. (See FAR 15.904(b) and FAR 52.215-31 for more information.)

### 5-701 Model Incurred Cost Proposal

The "Allowable Cost and Payment" clause (FAR 52.216-7) requires that the contractor prepare a proposal together with supporting data within 90 days after the end of its fiscal year. To assist contractors in meeting this requirement, this section of the pamphlet presents DCAA's model incurred cost proposal. The model includes example schedules on the following pages. These example schedules present the information needed to audit a contractor's proposal. If a contractor generates internal formal reports that identify the needed information, these internal reports can be submitted in lieu of the example schedules. However, the basic data contained in the schedules is required to complete the audit in a timely manner. The use of internal reports as a substitute for the example schedules formats shown should first be discussed with the contractor's cognizant DCAA field audit office.

Note that depending upon the size of the firm, complexity of the accounting system, and type of business, some of the information contained in the schedules may not be necessary to perform the audit. Specific requirements should be coordinated with the cognizant DCAA field audit office.

This model incurred cost proposal demonstrates only a final overhead and G&A rate. Some operations may have additional rates, such as: Fringe benefits rate, Engineering overhead rate, Manufacturing overhead rate, off-site rate, etc. A separate schedule should be prepared for each

final or intermediate indirect expense pool. If expenses are available by department (e.g., President's Office, Marketing Department for G&A; Fabrication, Assembly/Test for overhead), a breakout by expense for each department should also be provided.

DCAA prefers that contractors include an Index similar to that used in the model incurred cost proposal for each year submitted. If certain schedules are not applicable, the contractor should so note on the index.

In addition to the data presented in the schedules, there is additional information that the auditor typically needs to facilitate timely completion of the audit in accordance with generally accepted government auditing standards. A list of this information is presented on the page entitled "Supplemental Model Incurred Cost Proposal Information." Having this information available at the entrance conference will make the audit process as fast and efficient as possible.

The company name and fiscal period should be included on all schedules submitted. If Excel, Lotus 1-2-3, or other software programs were used to generate the schedules, the diskette containing the schedules should be included with the proposal or be made available to the auditor.

# Overhead Expenses Fiscal Year Ended 3/31/92

Account	Incurred Costs	Adjustments	Claimed Costs	Notes
Salaries and Wages	\$ 33,060	\$	\$ 33,060	
Postage Office Supplies	12,696	Ψ	. ,	
Other Outside Services	32,097		12,696 32,097	
Relocation	1,216	(777)	439	(1)
Business Meals	2,702	(111)	2,702	(1)
Telephone Expense	45,552		45,552	
Telecopier	2,434		2,434	
Equipment Rent	27,151		2,434 27,151	
Dues and Memberships	2,112	(500)	1,612	(2)
Depreciation/Amortization	2,824	(500)	2,824	(2)
Repairs and Maintenance	1,681		1,681	
Holiday	20,181		20,181	
Vacation	25,440		25,440	
Sick Leave	14,318		14,318	
Severance Pay	32,419	(23,023)	9,396	(2)
Employer FICA	23,612	(25,025)	23,612	(3)
FUI/SUI	7,023		7,023	
Workers' Compensation	3,311		7,025 3,311	
Health Insurance	31,097		31,097	
Life Insurance	6,833		6,833	
Pension Plan	58,320	(8,612)	49,708	(4)
Miscellaneous	2,513	(0,012)	<u>2,513</u>	(4)
Subtotal	388,592	\$(32,912)	355,680	
Occupancy Allocation (Sch C)	154,932	<del></del>	154,932	
Total Overhead Pool	\$ <u>543.524</u>	\$( <u>32,912)</u>	\$ <u>510.612</u>	
Overhead Base:				
Contract Labor (Sch F)	\$ 633,012	-	\$ 633,012	
IR&D Labor (Sch F)	14,287		14,287	(5)
B&P Labor (Sch F)	9,525		9,525	(5)
Total Overhead Base	\$ 656,824		\$ 656.824	(2)

Base - Straight time direct labor dollars of all contracts and projects including labor costs of IR&D/B&P projects.

OVERHEAD RATE <u>82.75</u>% <u>77.74</u>% (\$543,524÷ \$656,824) (\$510,612 ÷ \$656,824)

## **Explanatory Notes**

- (1) Moving charges in excess of those allowable by FAR 31.2.
- (2) Membership fees and tennis dues of one individual not allowable per FAR 31.2.
- (3) Severance pay in excess of amount approved and considered allowable by the ACO.
- (4) Employer contributions to pension plan in excess of that approved and considered allowable by the ACO.
- (5) The IR&D and B&P labor costs are included in the overhead base in order to allocate a proportionate share of overhead to the labor as required by FAR 31.2.

# General & Administrative (G&A) Expenses (See Note 10) Fiscal Year Ended 3/31/92

	Incurred		Claire at	
Account	Costs	A di a	Claimed	
Salaries and Wages	\$ 90,007	<u>Adjustments</u>	Costs	<u>Notes</u>
Professional Fees	34,105		\$ 90,007	
Travel	12,987	(1.305)	34,105	**
Entertainment	484	(1,295)	11,692	(1)
Advertising and Promotion	354	(484)	0	(2)
Bad Debts	3,018	(287)	67	(3)
Periodicals and Publications	6,435	(3,018)	0	(2)
Conventions and Seminars	7,936	(210)	6,435	(4)
Interest Expense	1,001	(319)	7,617	(1)
Holiday and Vacation	8,134	(1,001)	0	(2)
Sick Leave and Personal Absence			8,134	
Employee FICA	2,069		2,069	
FUI/SUI	3,815		3,815	
Health / Life Insurance	1,093		1,093	
Pension Plan	9,999		9,999	
Miscellaneous	12,318	(1,883)	10,435	(4)
Miscenaricous	3,873		3,873	
Occupancy Allocation (Sch C)	23,151		23,151	
IR&D Mat'l, Trvl, ODC (Sch F)	9,724		9,724	
IR&D Labor (Sch F)	14,287		14,287	
IR&D Overhead (Sch F)	11,822	(715)	11,107	(5)
B&P Mat'l, Tryl, ODC (Sch F)	6,485	(120)	6,485	(5)
B&P Labor (Sch F)	9,525		9,525	
B&P Overhead (Sch F)	7,882	(477)	7,405	(5)
IR&D/B&P Over ceiling (Sch H)	<del></del>	_(573)	( <u>573</u> )	(6)
Total G&A Expense Pool	\$ <u>280,504</u>	\$ <u>(10,052)</u>	\$ <u>270,452</u>	
G&A BASE:				
Contract direct costs (Sch F)				
Labor			\$633,012	
Travel	34,563			
Material	842,981			
Other direct costs	172,105			
Subcontracts	944,841			
Total direct costs	2,627,502			
Overhead (Sch B-1)	543,524	(7)		
Less: IR&D/B&P O/H transferred to	G&A:		343,324	(7)
IR&D O/H @ General Ledger Rate			(11 922)	(9)
B&P O/H @ General Ledger Rate	(11,822)	(8)		
Total G&A Expense Base			<u>(7,882)</u> \$ 3.151.322	(8) (9)
Base - Total cost input (excludes G&A	ID&D B&D and	Cost of Manage	* * * * * * * * * * * * * * * * * * * *	()
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G&A EXPENSE RATE	(\$270,452 ÷ \$3.151,322)		<u>8.58</u> %	

# **Explanatory Notes**

- (1) Expenses of the President, Vice President and their wives on a personal trip not claimed.
- (2) Unallowable cost per Government procurement regulation FAR 31.2.
- (3) Unallowable promotion expense; balance claimed is help-wanted employment advertising.
- (4) Employer contributions to pension plan in excess of that approved and considered allowable by the ACO.
- Overhead on IR&D/B&P labor is shown at the General Ledger rate of 82.75% (IR&D \$14,287 x .8275 = \$11,822) (B&P \$9,525 x .8275 = \$7,882). The adjustments reflect the difference between the General Ledger rate and the claimed rate applied to the IR&D/B&P labor.

- (6) See Schedule H for computation of allowable IR&D/B&P costs.
- (7) The claimed G&A/IR&D/B&P base must include both the Schedule B-1 claimed overhead (\$510,612) plus overhead costs incurred but not claimed (\$32,912).
- (8) Overhead on the IR&D/B&P labor at the 82.75% rate is added to the G&A pool (Schedule B-2) and deducted from the G&A base.
- (9) The total cost input base consists of contract direct costs plus overhead (claimed and unclaimed) less overhead on IR&D/B&P transferred to the G&A pool. The base does not include IR&D/B&P direct labor or other IR&D/B&P direct costs which are recovered through the G&A pool.
- (10) Although IR&D and B&P are technically not G&A expenses, they are normally allocated using the same cost input base as used for G&A. The term G&A as used in this model proposal includes IR&D and B&P. In the event that the base used to allocate IR&D and B&P is different than the base used to allocate G&A, a separate computation for IR&D and B&P would be required.